

Preventing Foreclosure

Initiatives to Sustain Homeownership

By Carolina Reid

In 2005, nearly 700,000 households entered the mortgage foreclosure process in the United States, and nearly 10 times as many households were behind on their mortgage payments.¹ While this represents a relatively low percentage of the total mortgages serviced, the costs of foreclosure can be substantial, and not only for the families who lose their homes. Research suggests that lenders can lose an average of \$44,000 to \$58,000 per completed foreclosure, depending on the circumstances.² And cities lose money too—estimates of losses to local municipalities range from \$400 to \$34,000 per foreclosure.³ Foreclosures may have other negative impacts as well, as vacant properties can become sites of crime and distress.⁴ Taken together, these consequences yield a strong rationale for lenders and local governments to work together with nonprofits and families to prevent foreclosure.

Within the Federal Reserve's 12th District, the issue of foreclosure prevention has not been as prominent as in some other parts of the country. The rapid rates of house price appreciation in California, Nevada, Arizona, Washington and Oregon have likely hidden borrower distress, since families delinquent on their mortgage payments have been able to sell their properties quickly and most likely at a profit. Overall, rates of delinquency and foreclosure in the 12th District are lower than the U.S. as a whole. Yet if the housing market

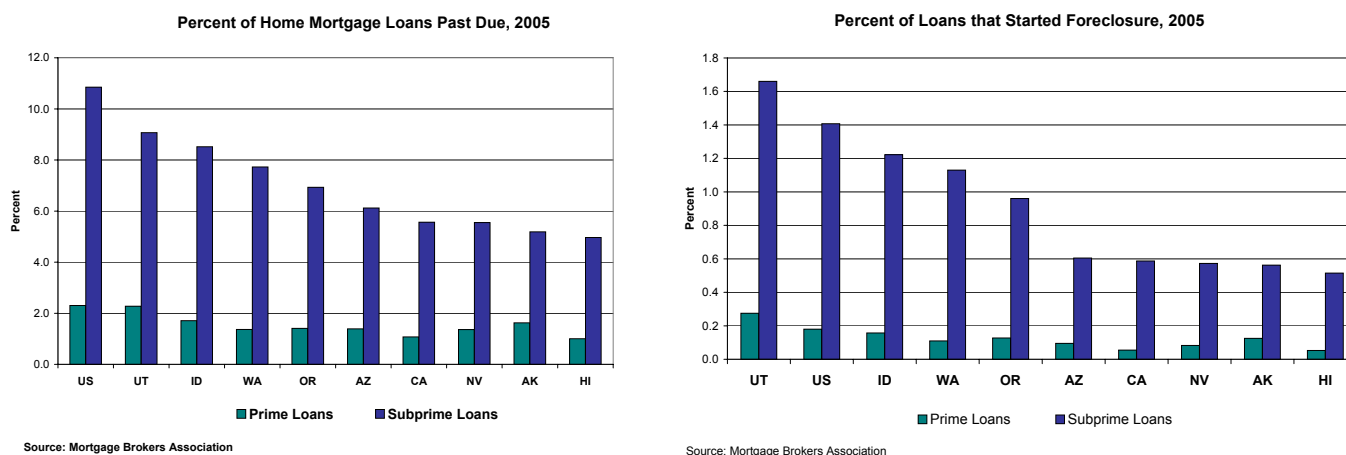
cools, and as adjustable-rate or interest-only mortgages reset, many borrowers may suddenly face mortgage default and foreclosure and risk losing the equity that they have gained. This is of particular concern for borrowers in the subprime market. (See Figure 2.1: Trends in Borrower Distress, The Federal Reserve's 12th District)

In this article, we look at some of the recent innovations in policies and programs across the country that address homeownership preservation. From pre-purchase homeownership counseling to state policies that help to limit predatory lending, these initiatives show the range of possible interventions and partners that can help to keep families in their homes. Expanding and replicating these efforts within the 12th District could help more families to keep their homes and to continue to build equity.

Pre-Purchase Counseling

Given the bewildering array of mortgage products available—and the potential for falling victim to predatory lenders—there is a clear need for more pre-purchase homeownership counseling that will help families successfully navigate the mortgage market. Evidence suggests that as many as one-third to one-half of subprime borrowers could qualify for prime loans. Many borrowers—particularly low-income and minority families who have been traditionally excluded

Figure 2.1 Trends in Borrower Distress, The Federal Reserve's 12th District



from access to credit—lack the information they need to choose the best mortgage product for their financial situation.⁵ For example, researchers have found that compared to prime borrowers, subprime borrowers are less knowledgeable about the mortgage process, less likely to search for the best mortgage rates, and less likely to be offered a choice among alternative mortgage terms and instruments.⁶

Pre-purchase homeownership counseling can help to mediate these information asymmetries and ensure that borrowers have the information they need to make good decisions. However, the evidence on the success of counseling is mixed.⁷ One of the difficulties of measuring the impact of counseling programs is that the quality of counseling can vary, and researchers have pointed out that there is an important distinction between providing information and providing education.⁸ Yet studies have found that counseling, particularly face-to-face counseling, can improve loan performance and lead to lower rates of delinquency and default.⁹ Increasing the amount of funding available for homeownership counseling would increase the reach and impact of these programs.

Across the country, there are a number of consumer education initiatives that are designed to inform borrowers, increase their financial literacy, and protect them from predatory lenders. The U.S. Department of Housing and Urban Development (HUD) certifies agencies throughout the country that provide homeownership counseling.¹⁰ Through these HUD-approved agencies, counselors are able to review loan disclosure statements with clients and assist them in understanding the terms and conditions of the loan they are considering. The Federal Housing Administration (FHA) also runs a Homebuyer Education Learning Program (HELP), which covers topics like budgeting, finding a home, getting a loan, and home maintenance. Completion of the program may entitle the homebuyer to a reduced initial FHA mortgage insurance premium.

For the vast majority of borrowers, however, education and counseling is only available if they seek it out proactively. One of the largest challenges facing the homeownership counseling field is reaching potential clients before they sign the loan documents. Increasingly, initiatives are developing large-scale marketing campaigns to educate consumers about mortgage lending. For example, to promote public awareness of predatory lending, Freddie Mac is rolling out a nationwide campaign called “Don’t Borrow Trouble”. In partnership with local governments and organizations, the campaign uses mailings, public service announcements, transit ads and television commercials to inform the public about predatory practices, and also provides referrals to counselors for additional support. (See Figure 2.2: “Don’t Borrow Trouble” Campaigns in the Federal Reserve’s 12th District)

In addition to educating consumers about the home buying process, a growing number of programs are focusing on post-purchase counseling, helping families *after* they’ve

“Don’t Borrow Trouble” Campaigns in the Federal Reserve’s 12th District

Alaska

Arizona

Pima County

California

Los Angeles

Oakland

Sacramento

San Francisco

San José/Silicon Valley

Nevada

Reno/Northern Nevada

Las Vegas/Southern Nevada

Washington

Seattle/King County

bought a home. In Minnesota, the Emerging Markets Homeownership Initiative (EMHI) provides an interesting model that integrates both pre-purchase and post-purchase elements in its effort to help increase the homeownership rate among “emerging market” households,¹¹ including minorities and new immigrants.¹² EMHI’s goal is to decrease racial and ethnic disparities in homeownership by addressing the barriers to homeownership that emerging market households face. But, rather than seeing homeownership as the end goal, EMHI’s business plan recognizes the need to sustain homeownership after initial purchase. The program will build on existing networks of service providers in Minnesota to provide training on home maintenance, household budgeting, and counseling on emerging debt or mortgage payment issues. The initiative is also looking at ways to offer households financial assistance, such as short-term loans to cover unanticipated expenses or income shortfalls, to keep them in homeownership.¹³

A Focus on Foreclosure Prevention

While counseling is clearly important, when families enter into mortgage default or foreclosure proceedings, a more intensive strategy is usually called for. Increasingly, nonprofit organizations and government agencies are partnering with lenders to develop foreclosure avoidance programs that work directly with distressed borrowers to help keep them in their homes. These programs generally combine public awareness and counseling components with mortgage workouts or rescue loans.

The Home Ownership Preservation Initiative (HOPI) in Chicago provides an excellent example of this approach. Launched in 2003 by Neighborhood Housing Services (NHS) of Chicago in partnership with the City of Chicago, the Credit Counseling Resource Center and private sector financial institutions, HOPI incorporates a public awareness campaign, phone and face-to-face counseling, loan workouts to help prevent foreclosure, and reclamation of foreclosed homes to restore them as neighborhood assets. Recognizing that one of the largest challenges is reaching distressed

In December 2003, Mr. Marigold² was at risk of losing his home of more than 20 years. A series of events—including unanticipated medical expenses and a refinancing based on a fraudulent appraisal—had left Mr. Marigold unable to make the payments on an 11.6 percent APR, \$67,500 loan, and unable to come up with the money to make the balloon payment of \$29,325 due in April. Rather than foreclosing on the property, however, Mr. Marigold's lender contacted the Consumer Rescue Fund (CRF). In collaboration with HSBC North America, the CRF was able to extend Mr. Marigold a loan of \$77,000—enough to cover both the previous loan and the balloon payment—at a low APR of 6.99 percent, and keep him in his home.

Mr. Marigold's story illustrates how the CRF can help borrowers who are at risk of foreclosure due to predatory loans. Launched by the National Community Reinvestment Coalition in 2001, the CRF has helped more than 1,000 consumers in 17 states preserve their homes.³ The program is built on a strong partnership between NCRC, its member organizations, and HSBC North America. Often, the first line of defense is NCRC's member organizations, predominately housing counselors and community development corporations that work in the community. Through these community partners, NCRC's Fair Lending specialists learn about families facing foreclosure and review their loan documents including the Good Faith Estimate and income verification statements.

If the specialists conclude that the loans are predatory, there are a number of options to help the consumer, including:

- **Mediation.** NCRC will work directly with the lender or servicer to have abusive terms eliminated and to prevent foreclosure proceedings.
- **An affordable refinance loan.** NCRC has partnered with HSBC North America, which refinances the loans of predatory lending victims. The predatory loans are replaced with market-rate or below market-rate loans, and do not contain prepayment penalties, balloon payments, or credit insurance.
- **Litigation.** If NCRC discovers a pattern and practice of abusive lending or servicing on the part of a financial institution, NCRC will pursue legal redress and file a complaint with the Department of Housing and Urban Development.
- **Financial education.** NCRC will provide consumers with financial education as part of their case management work, guiding them through the remediation process and coaching them on how to avoid predatory lending situations in the future.

The CRF has had a significant impact on helping to preserve homeowner equity. A recent analysis shows that CRF rescue loans have helped to lower families' interest rates by an average of 3.84 percent, decreasing their monthly payments by an average of \$275 dollars. Particularly for low-income families, this reduction in the cost of credit can provide enormous benefits to household financial well-being and greatly increase the likelihood that they will keep their homes.

According to Josh Silver, the Vice President of Research and Policy at NCRC, one of the key challenges for CRF moving forward is to expand the scale at which the program operates. "We know that predatory practices are increasing, and we have a successful model that can help families preserve wealth," said Silver. "What we'd like to see now is the participation of additional lenders in the program, and to expand our reach in states like California and Nevada."

borrowers, HOPI launched a mortgage default hotline using Chicago's non-emergency "311" telephone service. In addition, the City of Chicago sent 25,000 postcards promoting counseling to targeted zip codes, and used public service announcements, media events and bus and subway advertisements to reach borrowers. To fund the initiative, NHS created a capital pool by establishing mortgage-backed certificates, funded with a three-year, \$100 million commitment from Chicago's financial community and \$3 million from the city's CDBG fund.¹⁴ During the three year HOPI pilot phase, the program provided counseling and education to more than 4,300 families in Chicago, and helped to pre-

vent the foreclosure of more than 1,300 homes.¹⁵

NeighborWorks America, NHS's parent organization, recently launched the Center for Foreclosure Solutions to expand the HOPI model nationally. Beginning in Ohio, the Center is supporting a coordinated foreclosure prevention and intervention strategy in communities nationwide. The strategy entails a widespread public outreach campaign. In partnership with the Homeownership Preservation Foundation, the Center promotes a toll-free hotline (1-888-995-HOPE) that offers free foreclosure prevention services and counseling to consumers. In addition to raising public awareness, the Center is working to build the capac-

Financial institutions are important partners in efforts to help preserve homeownership, particularly among low- and moderate-income borrowers. Banks can receive CRA consideration for financial contributions that fund nonprofit credit counseling agencies that advise low- or moderate-income borrowers on homeownership issues. For example, financial contributions to programs like Chicago's HOPI "311" hotline and Freddie Mac's "Don't Borrow Trouble" can be CRA eligible when they help low- or moderate-income borrowers by providing financial counseling. Financial contributions from banks that help capitalize loan-rescue funds for low- or moderate-income borrowers mired in predatory loans can also receive CRA consideration. Participation in a loan-rescue fund that is part of a municipal plan to revitalize and stabilize a low- or moderate-income geography would also be viewed positively under CRA.

In addition, when banks must take a deed in lieu of foreclosure, the property can be donated, or sold at a discounted price, to a nonprofit community development organization for a qualified CRA purpose, such as providing affordable housing for low- or moderate-income homebuyers. For example, a bank could donate a vacant house to a nonprofit organization that would rehabilitate the property and sell it to a low- or moderate-income family for affordable housing. The transfer of such a property, when part of a formal revitalization and stabilization plan, also can help stabilize low- or moderate-income neighborhoods when the nonprofit resells the home to new residents, preventing further neighborhood deterioration.

Adapted from Karen Tucker (2006), "Compliance Corner—Homeownership: Preserving the American Dream", The Office of the Comptroller of the Currency *Community Development Investments Online*.

ity for foreclosure counseling at the local level, and is using research to help identify local "hotspots"—areas that are experiencing a high concentration of foreclosure activity—for targeted interventions.

Other organizations are also taking the lead on helping families and communities prevent foreclosure. The Consumer Rescue Fund, spearheaded by the National Community Reinvestment Coalition, focuses on helping families that have fallen victim to predatory loans. (See Box 2.1: The Consumer Rescue Fund) ACORN Housing—with local offices in Arizona, California, Nevada, Oregon and Washington—has similarly launched a nationwide foreclosure mitigation program.¹⁶ Financial institutions—in addition to helping to fund a wide range of foreclosure prevention activities—have also begun to examine ways to help their own borrowers. (See Box 2.2: Asset Preservation Efforts and the Community Reinvestment Act) JPMorgan Chase, for example, has established a Homeownership Preservation Office designed specifically to help Chase mortgage customers who are delinquent or at risk of foreclosure.¹⁷

State and local governments are also developing innovative programs to help borrowers who are facing foreclosure. Perhaps the only program of its kind in the nation, Pennsylvania's Homeowners Emergency Mortgage Assistance Program (HEMAP) provides distressed borrowers with loans that bring their delinquent mortgage payments current to a specified date. For those who qualify, the program also offers continuing loans that subsidize borrowers' monthly mortgage payments for a set time period. Counseling agencies work out forbearance agreements with lenders and also counsel families regarding their financial situations. The program is funded by both state appropriations and the repayment of HEMAP loans.¹⁸

State and Federal Policies and Regulations

While pre- and post-purchase counseling and foreclosure prevention initiatives are valuable components of a homeownership preservation strategy, there is also a place for policies and regulations that prohibit predatory lending practices. Certain lending practices, such as prepayment penalties and balloon payments, are more likely to lead to foreclosures than loans without those terms, even after controlling for key risk factors such as credit scores. Predatory lending—particularly with fraudulent intent—is a particularly serious problem that disproportionately affects low-income and minority borrowers. In these instances, access to credit works in direct opposition to the goals of asset building and community revitalization, and requires more intervention than just additional counseling.

Congress has enacted a wide range of federal laws and subsidy programs that affect the provision of credit and that serve to regulate and prohibit abusive lending practices. Michael Barr has usefully distinguished between the different regulations in the following way:¹⁹

- **Affirmative obligation**, like the Community Reinvestment Act (CRA), which encourages federally insured banks and thrifts to meet the credit needs of the entire communities that they serve, including low- and moderate-income areas;
- **Negative prohibition**, like the Equal Credit Opportunity Act (ECOA), which prohibits creditors from discrimination based on "race, color, religion, national origin, sex or marital status, or age";
- **Disclosure**, which can either serve to inform the consumer, like the Truth in Lending Act (TILA), or which

can increase the ability of the public, regulators, and fair lending enforcement agencies to assess whether lenders are engaged in discriminatory practices, like the Home Mortgage Disclosure Act (HMDA); and

- **Product regulation**, like the Home Ownership and Equity Protection Act (HOEPA), which imposes product restrictions on certain categories of loans.

Barr also notes that subsidies, such as government insurance through the Federal Housing Administration and flexible underwriting criteria for loan purchases by Fannie Mae and Freddie Mac, can influence the supply of credit for homeownership. As a whole, these regulations and subsidies have helped to increase access to credit in low-income and minority communities, combat discrimination, and address market failures. And as Barr points out, these laws can reinforce one another; for example, disclosure laws can be used to enhance negative prohibitions regarding racial discrimination.²⁰

Yet, many advocates and researchers argue that existing regulations don't go far enough in protecting consumers. Some note that TILA, for example, has not lived up to its goal of standardizing disclosures on the total cost of credit, since many closing costs are currently excluded when computing finance charges and annual percentage rates.²¹ HOEPA, while placing restrictions on high-cost loans, does not apply to home purchase mortgages. HOEPA's triggers have also come under critique as being too high.²² The challenge for policy-makers, however, is to balance the desire for consumer protection with the desire to provide broad access to credit, particularly among low-income and minority borrowers. Determining the right level of intervention is particularly difficult in high-cost real estate markets like California, where many families wouldn't be able to get into homeownership at all without taking on high debt-to-income ratios or using nontraditional mortgage products.


Still, as the use of alternative mortgage products and subprime loans has grown, regulators and consumer advocates have expressed concern that consumers may not understand the risks of these products, and that there is a need to improve the clarity and comprehensiveness of disclosures.²³ The federal banking regulators recently issued interagency guidance on alternative mortgage product lending that discusses underwriting guidelines, portfolio and risk management, and consumer disclosure practices. (See article: Non-traditional Mortgage Guidance) The Federal Reserve Board is also in the process of an extensive review of Regulation Z, and is considering changes to both the content and format of mortgage disclosures to improve their effectiveness.²⁴ Legislative bills with varying degrees of control on predatory lending activities are also likely to be introduced during the 110th Congress.²⁵

In the absence of additional federal regulations prohibiting predatory lending, some states and municipalities have developed local legislation that sets lower triggers than HOEPA, requires additional disclosures, and/or bans a broader array of abusive practices.²⁶ For instance, some prohibit prepayment penalties, limit broker "kickbacks" and excessive fees, restrict loan flipping, and ensure that homeowners have a right to pursue meaningful remedies against foreclosure. As of September 2006, 28 states had enacted laws to restrict predatory lending, including California, Nevada, and Utah in the Federal Reserve's 12th District.^{27,28}

State laws restricting predatory lending practices vary in their design and stringency, and advocates like the Center for Responsible Lending are encouraging more states to develop legislation similar to that adopted in North Carolina. In 1999, North Carolina became the first state to enact legislation to curb predatory mortgage lending. Research assessing the impact of this legislation has been largely favorable, although not universally so. Two studies, using a subset of loan data from nine lenders, cite a decline in subprime mortgages in North Carolina and argue that reductions in predatory lending had been attained at the expense of legitimate subprime lending activity, particularly to low-income borrowers.²⁹

Other researchers using larger datasets, however, have found that the reduction in subprime lending has been beneficial to consumers, in that the law has removed the riskiest loans without a concomitant decline in access to homeownership for low-income borrowers.³⁰ Researchers at the University of North Carolina, for example, found that from 1998 to 2002, North Carolina did see a reduction in subprime lending, but that the effect was almost entirely in refinance mortgages, with almost 90 percent of the decline attributable to a reduction in predatory loans.³¹ As the researchers conclude, the experience in North Carolina shows that it is possible to develop laws that combat predatory lending without unduly restricting the flow of subprime mortgage credit.

Conclusion

In recent years, increasing the opportunity for homeownership has been a policy priority at the federal, state and local level; within this context, high cost loans and elevated foreclosure risk are in direct conflict with the vision of homeownership as an asset-building opportunity for households and a stabilizing force in communities. Failure to protect consumers from predatory lending and prevent avoidable foreclosures could undermine much of the success that has been achieved in increasing the number of low-income and minority households that are now homeowners. Developing a comprehensive strategy to help sustain homeownership—particularly among low-income and minority homeowners—will ensure that homeownership remains a key vehicle for household financial security and neighborhood stability. 

Homeownership at High Cost: Recent Trends in the Mortgage Lending Industry

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- 11 Johnson, Hans and Amanda Bailey (2005). "California's Newest Homeowners: Affording the Unaffordable," Public Policy Institute of California.
- 12 Because many of the AMP loans originated in recent years have not yet reset, it is not yet clear how much of an impact these types of payment shocks are having on delinquencies and foreclosure rates.
- 13 Apgar, William and Mark Duda (2005). *Collateral Damage: The Municipal Impact of Today's Mortgage Foreclosure Boom*. Report prepared for the Homeownership Preservation Foundation. Available: http://www.hpfonline.org/PDF/Apgar-Duda_Study_Final.pdf
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- 15 Immergluck, Daniel and Geoff Smith (2005). "The Impact of Single-Family Mortgage Foreclosures on Neighborhood Crime." Paper presented at the Federal Reserve System National Community Affairs Research Conference, Washington, D.C.
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Lending: An Overview" http://www.knowledgeplex.org/kp/text_document_summary/article/refiles/hot_topics/Carr-Kolluri.pdf

- 18 Loans are identified as "high cost" in the Home Mortgage Disclosure Act (HMDA) dataset if the spread between the interest rate on the loan and the prime rate exceeded a specified amount (i.e. 3% for first-lien loans and 5% for second-lien loans).
- 19 Avery, Robert, Kenneth Brevoort and Glenn Canner (2006). "Higher-Priced Home Lending and the 2005 HMDA Data." *Federal Reserve Bulletin*. Federal Reserve Board.
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- 21 Courchane, Marsha, Brian Surette and Peter Zorn (2004). "Subprime Borrowers: Mortgage Transitions and Outcomes," *Journal of Real Estate Finance and Economics*, 29:4, 365-392, 2004.
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12th District Trends in Mortgage Lending – Box 1.1

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- 2 *FDIC Outlook Summer 2006—Breaking New Ground in U.S. Mortgage Lending*. Federal Deposit Insurance Corporation (2006). http://www.fdic.gov/bank/analytical/regional/ro20062q/na/2006_summer04.html
- 3 *Ibid.*

Predatory Lending – Box 1.2

- 1 "Loan flipping" refers to lenders who encourage borrowers to rapidly refinance loans; loan flipping may result in equity-stripping because refinancing costs money and often these charges are refinanced into the amount of the loan.

Foreclosure Risk in California – Box 1.3

- 1 This research focuses on a subset of the subprime market—loans that are "high cost." For the first time in 2004, loans are identified as "high cost" in the Home Mortgage Disclosure Act (HMDA) dataset if the spread between the interest rate and the prime rate exceeded a specified amount (i.e. 3 percent for first-lien loans and 5 percent for second-lien loans).
- 2 According to a recent study by the Public Policy Institute of California, forty percent of households with mortgages in the state, and 52 percent of recent homebuyers pay more than the HUD recommended guideline of spending 30 percent of their income on housing costs. Twenty percent spend more than half of their income on their housing costs. Among low-income households, the percentages of those spending the majority of their income on housing costs is even higher. Baldassare, M. "Statewide Survey November 2004: Special Survey on Californians and Their Housing," Public Policy Institute of California. Available at: http://www.ppic.org/content/pubs/survey/S_1104MBS.pdf
- 3 Notices of Default are not a perfect indicator of foreclosure risk because many households that have home loans they cannot afford do not ever get to the point where they receive a notice of default. Some homeowners are able to refinance or sell their home before receiving this official warning. Here, the term "foreclosure risk" is used as shorthand to describe areas in which households have received notices of default. Areas are described as having a "higher level of foreclosure risk" if they have a higher rate of notices of default.

Preventing Foreclosure: Initiatives to Sustain Homeownership

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- 7 Apgar W. C. and Fishbein, A.J. (2005). Hilgert, M.A., Hogarth J.M., & Beverly S.. (2003). "Household Financial Management: The Connection between Knowledge and Behavior." *Federal Reserve Bulletin*, 89 (7) 309-322. M. Wiranowski, 2002, *Sustaining Home Ownership Through Education and Counseling*. Joint Center for Housing Studies, Harvard University.
- 8 Hilgert, M.A., Hogarth J.M., & Beverly S. (2003).
- 9 Hirad, A. and Zorn, P. (2001). *A Little Knowledge is a Good Thing: Empirical Evidence of the Effectiveness of Pre-Purchase Homeownership Counseling*. Hartarska, V., Gonzalez-Vega, C., and Dobos, D. (2002). *Credit Counseling and the Incidence of Default on Housing Loans by Low-Income Households*.
- 10 For a list of organizations and agencies that provide HUD certified homeownership counseling in your state, visit <http://www.hud.gov/offices/hsg/sfh/hcc/hcs.cfm>.
- 11 Emerging markets are defined as households of color, non-English speaking households, and households in which English is a second language.
- 12 Todd, R. and Grover, M. (2005). "A Case for Post-Purchase Support Programs as Part of Minnesota's Emerging Markets Homeownership Initiative," *Federal Reserve Bank of Minneapolis Community Affairs Report No. 2005-1*.
- 13 For more information on EMHI's goals and participating organizations, see the EMHI Business Plan at www.mhfa.state.mn.us/about/EMHI_Business_Plan.pdf.
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- 15 Neighborhood Housing Services of Chicago (2006). *Home Ownership Preservation Initiative: Partnership Lessons & Results, Three Year Final Report*.
- 16 For more information on ACORN's HFC Foreclosure Avoidance Program, please visit <http://acornhousing.org/TEXT/fap.php>.
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- 23 United States Government Accountability Office (2006). *Alternative Mortgage Products: Impact on Defaults Remains Unclear, but Disclosure of Risks to Borrowers Could be Improved*. GAO-06-1021.
- 24 S.F. Braunstein (2006). *Nontraditional mortgage products*. Testimony before the Subcommittee on Housing and Transportation and the Subcommittee on Economic Policy, Committee on Banking, Housing, and Urban Affairs, U.S. Senate, September 20, 2006.
- 25 For an analysis of the differences between HR 1182, Prohibit Predatory Lending Act (Miller-Watt-Frank) and HR 1295, Responsible Lending Act (Ney-Kanjorski), the two pieces of legislation introduced during the 109th Legislative Session, visit <http://www.responsiblelending.org/issues/mortgage/policy/page.jsp?itemID=29837365>
- 26 Quercia, R.G., Stegman, M.A., and Davis, W.R. (2004). "Assessing the Impact of North Carolina's Predatory Lending Law," *Housing Policy Debate* 15(3): 573-601.
- 27 Other states with predatory lending laws include Arkansas, Colorado, Connecticut, the District of Columbia, Florida, Georgia, Illinois, Indiana, Kentucky, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New Mexico, New York, North Carolina, Ohio, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Tennessee, Texas, and Wisconsin.
- 28 Information relating to state and local laws and their provisions is from a database maintained by Butera & Andrews, A Washington, D.C., law firm that tracks predatory lending legislation, and is current as of September 8, 2006.
- 29 Elliehausen, G. and Staten, (2002) *Regulation of Subprime Mortgage Products: An Analysis of North Carolina's Predatory Lending Law*, Credit Research Center, Georgetown University.
- 30 For a review of these studies, see Quercia, R.G., Stegman, M.A., and Davis, W.R. (2004).
- 31 Quercia, R.G., Stegman, M.A., and Davis, W.R. (2004).

The Consumer Rescue Fund – Box 2.1

- 1 For a more detailed description and analysis of the Consumer Rescue Fund, see Josh Silver and Marva Williams (2006), *Asset Preservation: Trends and Interventions in Asset Stripping Services and Products*, National Community Reinvestment Coalition and The Woodstock Institute.
- 2 The name of the consumer has been fictionalized for privacy reasons.
- 3 Alabama, Arizona, California, Florida, Georgia, Illinois, Indiana, Maryland, Massachusetts, Nevada, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, Texas, and Wisconsin.

Calculated Risk: Assessing Nontraditional Mortgage Products

- 1 This article was adapted from testimony that was given in September 2006 before the Senate Committee on Banking Housing and Urban Affairs. The full text is available at: <http://www.responsiblelending.org/policy/testimony/page.jsp?itemID=30380832>
- 2 Inside B&C Lending, 9/1/2006; See also Inside Mortgage Finance MBS Database, 2006.
- 3 54.7 percent of African-Americans who purchased homes in 2005 received higher-rate loans. 49.3 percent received such loans to refinance their homes.
- 4 46.1 percent of Latino white borrowers received higher-rate purchase loans. 33.8 percent received higher-rate refinance loans. For the purpose of this comment, "Latino" refers to borrowers who were identified as racially white and of Latino ethnicity.
- 5 Hudson, Mike and E. Scott Reckard, "More Homeowners with Good Credit Getting Stuck in Higher-Rate Loans," *L.A. Times*, p. A-1 (October 24, 2005).
- 6 *Ibid.*
- 7 In 2nd quarter of 2006, 80.7 percent of subprime loans were adjustable rate loans. This figure based on Mortgage Backed Securities through the 2nd quarter of 2006, see Inside Mortgage Finance MBS Database, 2006.
- 8 *Ibid.*
- 9 Laing, Jonathan R. "Coming Home to Roost," *Barron's* (New York, NY), Feb. 13, 2006, at 26.
- 10 For example, a recent prospectus shows that a large subprime lender, Option One underwrites to the lesser of the fully indexed rate or one percentage point over the start rate. For a loan with a typical 2/28 structure, the latter would always apply. See Option One Prospectus, Option One Mtg Ln Tr Asset Bk Ser 2005 2 424B5 May 3 2005, S.E.C. Filing 05794712 at S-50.
- 11 See, eg., Chase Home Finance Subprime Lending marketing flier, "Attractive Underwriting Niches," at www.chaseb2b.com (available 9/18/2006) stating "Taxes and Insurance Escrows are NOT required at any LTV, and there's NO rate add!" (suggesting that failing to escrow taxes is an "underwriting highlight" that is beneficial to the borrower).
- 12 See, eg., "B&C Escrow Rate Called Low" (February 23, 2005) *Mortgage Servicing News Bulletin*, July 23, 2005 "Servicers of subprime mortgage loans face a perplexing conundrum: only about a quarter of the loans include escrow accounts to ensure payment of insurance premiums and property taxes, yet subprime borrowers are the least likely to save money to make such payments....Nigel Brazier, senior vice president for business development and strategic initiatives at Select Portfolio Servicing, said only about 25 percent of the loans in his company's subprime portfolio have escrow accounts. He said that is typical for the subprime industry."
- 13 Mortgage Asset Research Institute, Inc, *Eighth Periodic Mortgage Fraud Case Report to Mortgage Bankers Association*, p. 12, available at <http://www.mari-inc.com/pdfs/mba/MBA8thCaseRpt.pdf> (April 2006).
- 14 Figure based on Mortgage Backed Securities through the 2nd quarter of 2006, see Inside Mortgage Finance MBS Database, 2006.
- 15 See "Steep Increase in California Foreclosure Activity," *DataQuick News*, October 18, 2006, <http://www.dqnews.com/RRFor1006.shtm> and "National Foreclosures Increase 17 Percent In Third Quarter" Press Release from RealtyTrac, November 1, 2006, <http://www.realtytrac.com/ContentManagement/PressRelease.aspx?ItemID=1362>.
- 16 Quercia, Roberto, Michael Stegman and Walter Davis, *The Impact of Predatory Loan Terms on Subprime Foreclosures: The Special Case of Prepayment Penalties and Balloon Payments*, Center for Community Capitalism, University of North Carolina at Chapel Hill (January 25, 2005) at 30 and 24.
- 17 CRL conducted an OLS regression of state-level changes in housing prices and foreclosure rates among subprime loans originated in 2000 (based on performance through May 2005), which shows a highly significant relationship ($p < 0.01$) with an adjusted r -squared of 0.57 and coefficient of -0.92. In other words, for every percentage point decrease in appreciation rates, the model predicts a 0.92 percentage point increase in foreclosure rates. Mean foreclosure rate=13.57 percent, $N=51$.
- 18 Knox, Noelle and Barbara Hansen, "More Fall Behind on Mortgages," *USA Today* at B1 (September 14, 2006). The *USA Today* figures refer to total delinquency figures (30 days + delinquent through foreclosure).
- 19 See MBA survey cited in Noelle Knox and Barbara Hansen, More Fall Behind on Mortgages, *USA Today* at B1 (September 14, 2006).
- 20 Income verification could include nontraditional methods including bank accounts, records of consistent bill paying that are not recorded by standard credit agencies or other methods that will reasonably verify income to meet mortgage requirements.

Nontraditional Mortgage Guidance

- 1 The guidance was issued by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the National Credit Union Administration. The guidance is available online at <http://www.federalreserve.gov/boarddocs/press/bcreg/2006/20060929/attachment1.pdf>.
- 2 Interagency Guidance on Subprime Lending, March 1999. <http://www.federalreserve.gov/boarddocs/srLETTERS/1999/sr9906a1.pdf>
- 3 February 14, 2006 letter to the Agencies. http://www.federalreserve.gov/SECRS/2006/February/20060224/OP-1246/OP-1246_10_1.pdf
- 4 See http://www.csbs.org/AM/Template.cfm?Section=Press_Releases&Template=/CM/ContentDisplay.cfm&ContentID=9010.

Comments on Interagency Guidance on Nontraditional Mortgages – Box 4.1

- 1 See http://www.federalreserve.gov/generalinfo/foia/index.cfm?doc_id=OP%2D1246&doc_ver=1&ShowAll=Yes.

Glossary

- 1, 2, 6, 7, 19: "Consumer Handbook on Adjustable Rate Mortgages" (2005). Board of Governors of the Federal Reserve System: http://www.federalreserve.gov/pubs/arms/glossary_english.htm.
- 13, 29: Board of Governors of the Federal Reserve System: <http://www.federalreserve.gov/events/publichearings/hoepa/2006/default.htm>
- 12: "Frequently Asked Questions about the New HMDA Data" (2006). Board of Governors of the Federal Reserve System: www.federalreserve.gov/boarddocs/press/bcreg/2006/20060403/attachment.pdf
- 3, 4, 5, 11, 16, 23, 25, 27, 30-33: Center for Responsible Lending: <http://www.responsiblelending.org/glossary.html>
- 8, 9, 10, 15, 18, 24: Fannie Mae: <http://www.fanniemae.com/tools/glossary.html>
- 14, 21, 22, 28: "Overview of Nonprime Mortgage Lending and Nontraditional Mortgage Product Terms". In FDIC Outlook Summer 2006—Breaking New Ground in U.S. Mortgage Lending. Federal Deposit Insurance Corporation: http://www.fdic.gov/bank/analytical/regional/ro20062q/na/2006_summer04.html
- 17, 20, 27: U.S. Department of Housing and Urban Development: <http://www.hud.gov/offices/hsg/sfh/buying/glossary.cfm>